

# **Builders' Use of Incentives Falls Back to 2002 Levels**

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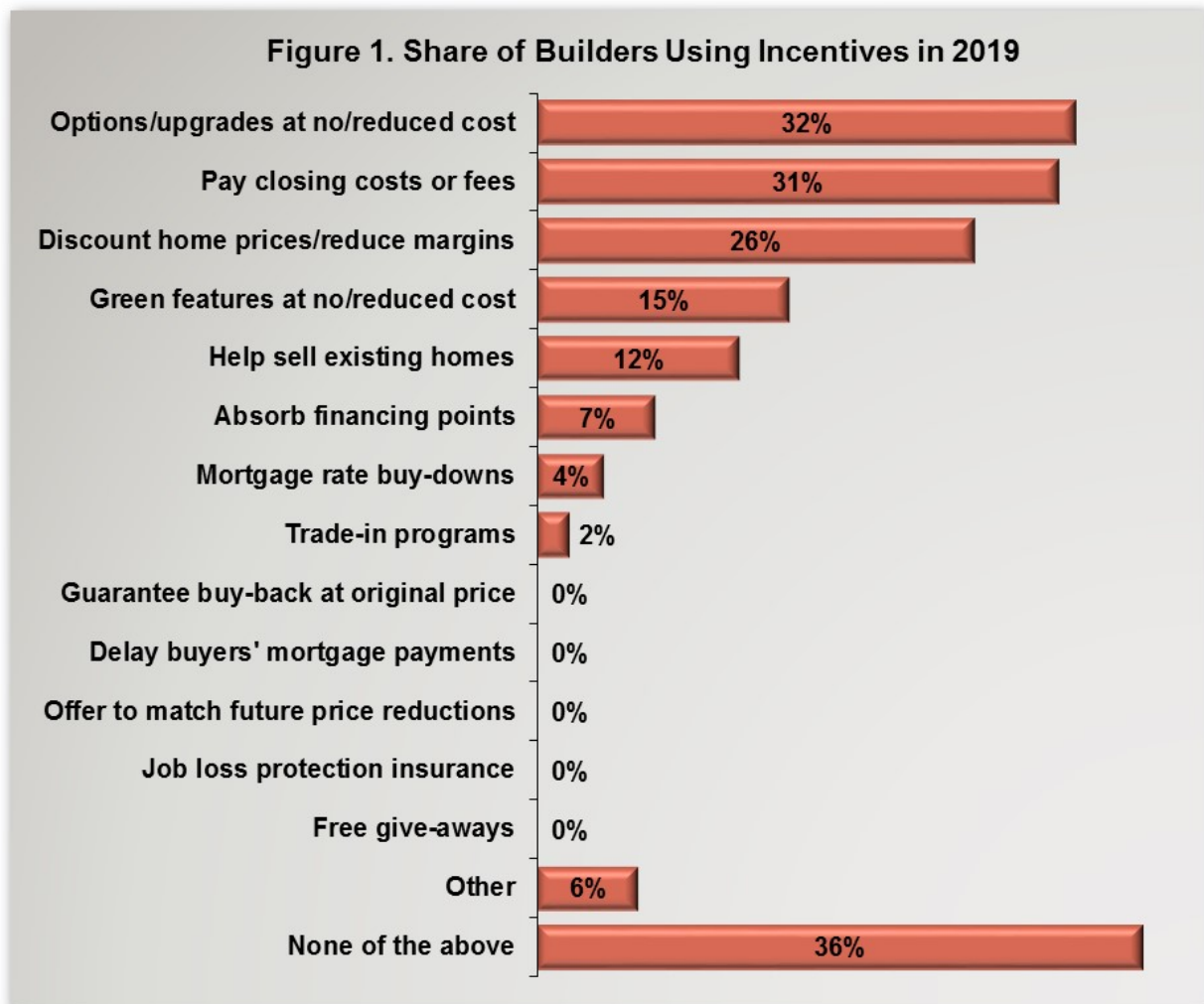
For many years it has been standard practice for some builders to offer special incentives to help boost sales when advertising their new homes. Common examples include builders offering options or upgrades at no or reduced cost and offering to pay closing costs or fees for their home buyers.

NAHB has regularly tracked builder use of these incentives in its monthly survey for the [NAHB/Wells Fargo Housing Market Index](#) (HMI). Results from various HMI surveys conducted over the years show that builders' use of many incentives skyrocketed during the housing downturn of 2007-2009, but has now declined to the point of being roughly consistent with industry practice before the 2003-2006 boom period and severe downturn that followed it. The sections below describe these trends in more detail.

## **Latest Results**

After a pause in recent years to focus on some of the issues (e.g., shortages of labor and subcontractors - July 3, 2014 Special Study) that emerged as the market was going through a period of steady (albeit modest) recovery, NAHB's HMI survey returned to the topic of sales incentives in April of 2019. Results from the 2019 survey show that the most common incentive currently being offered (by 32 percent of builders) is upgrades or other options at reduced or no cost, followed closely by paying closing costs (31 percent) and discounted home prices (26 percent). Energy-efficiency or green features at reduced or no cost are being offered by 15 percent of builders (fig. 1). It may seem that energy-efficiency/green features would be captured in the upgrades or other options that appear at the top of the figure. However, written comments from builders have made it clear over the years that many of them view green

features as a category unto itself. Since 2012, the HMI survey has listed green features at no or reduced cost as a separate incentive.



At the other end of the scale, none of the builders captured in the 2019 survey reported guaranteeing to buy back a home at its original price, delaying a buyer's mortgage payments, offering to match future price reductions, providing job loss insurance, or giving away free items (such as cars or vacations). Thirty-six percent of builders said that they used no special sales incentives at all.

## **Incentives in Historic Perspective**

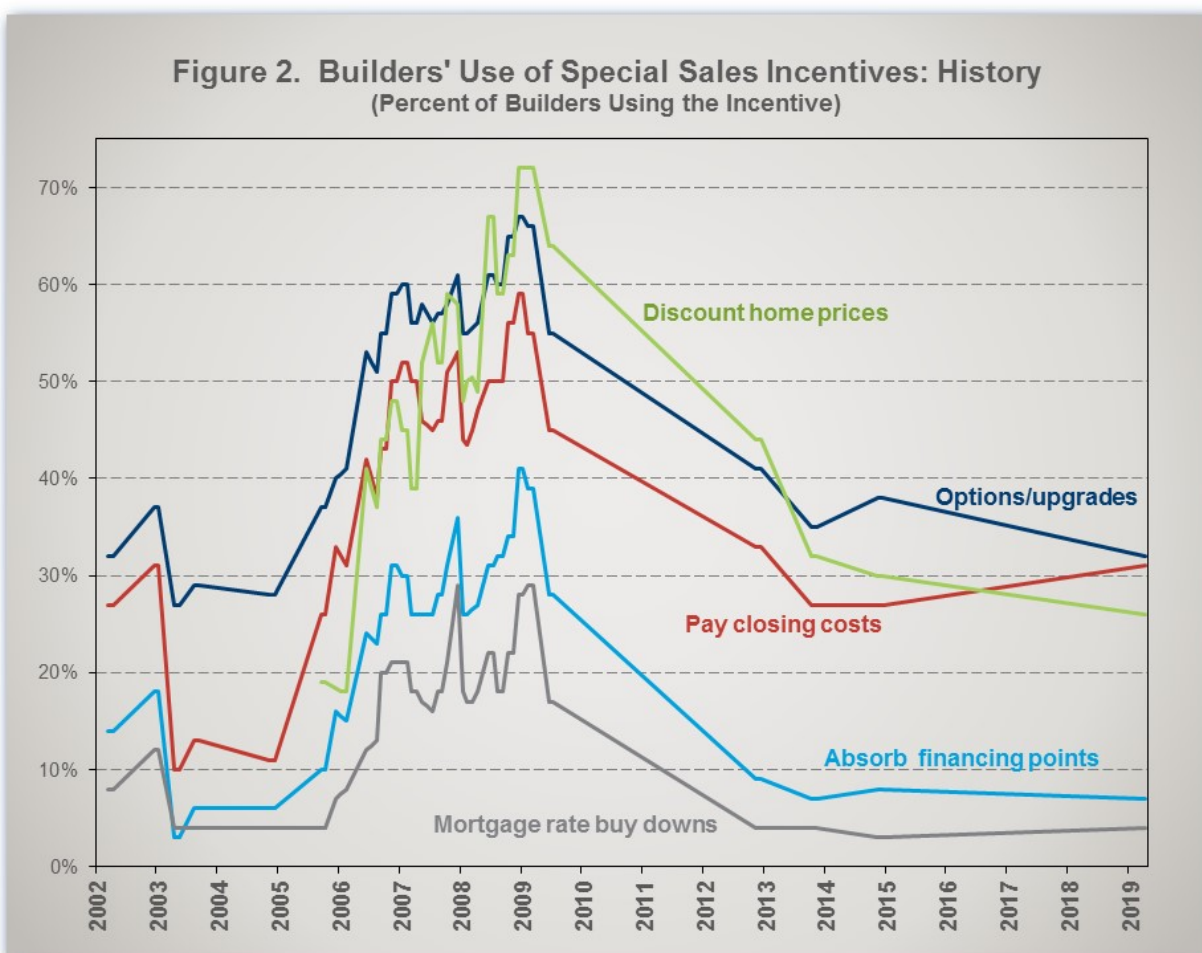
As anecdotal information about industry practices accumulated, NAHB added different incentives to its list over the years. As a result, interpretation of the “none of the above” category has not remained perfectly consistent. Nevertheless, even with that caveat in mind, it is notable that the share of builders not using any incentives in 2019 is comparable to the figure in March of 2002—38 percent. In between, the share not using incentives reached a high of 50 percent in the middle of 2003 (when annual housing starts broke above the 1.8 million mark for the first time since 1986 where they remained throughout the 2003-2006 boom), and a low of 14 percent at the end of 2008 (when starts dipped below 1.0 million for the first time since World War II, where they lingered until 2014).

Although the questionnaire has been modified somewhat, NAHB’s HMI survey has covered many of the more common sales incentives in a consistent fashion since the 1990s. Individually, each tells a similar story—with use declining to a trough in 2003-2004, then rising to an all-time high point at the end of 2008, before declining again to the point where it is now: about the same as it was before the boom and downturn took place.

Offering options/upgrades at no or reduced cost has traditionally been the most widely used sales incentive. Thirty-two percent of builders reported using it in March of 2002—exactly the same as in April of 2019. In between, however, the percentage varied substantially, declining to under 30 percent throughout 2003 and 2004 before ratcheting its way upward in fits and starts to a peak of 67 percent by the end of 2008.

Similarly, 27 percent of builders reported “paying closing costs” in March 2002, but by December of that year the share increased to 31 percent (the same as in April 2019) before plummeting to under 15 percent throughout 2003 and 2004, then rising to a peak of 59 percent in December 2008. “Absorbing financing points” crossed its current level of 7 percent on its way downward between 2002 and 2003, then reached a peak of 41 percent, also in December 2008. “Mortgage rate buy downs” are now about as uncommon as they have ever been, used by only 4

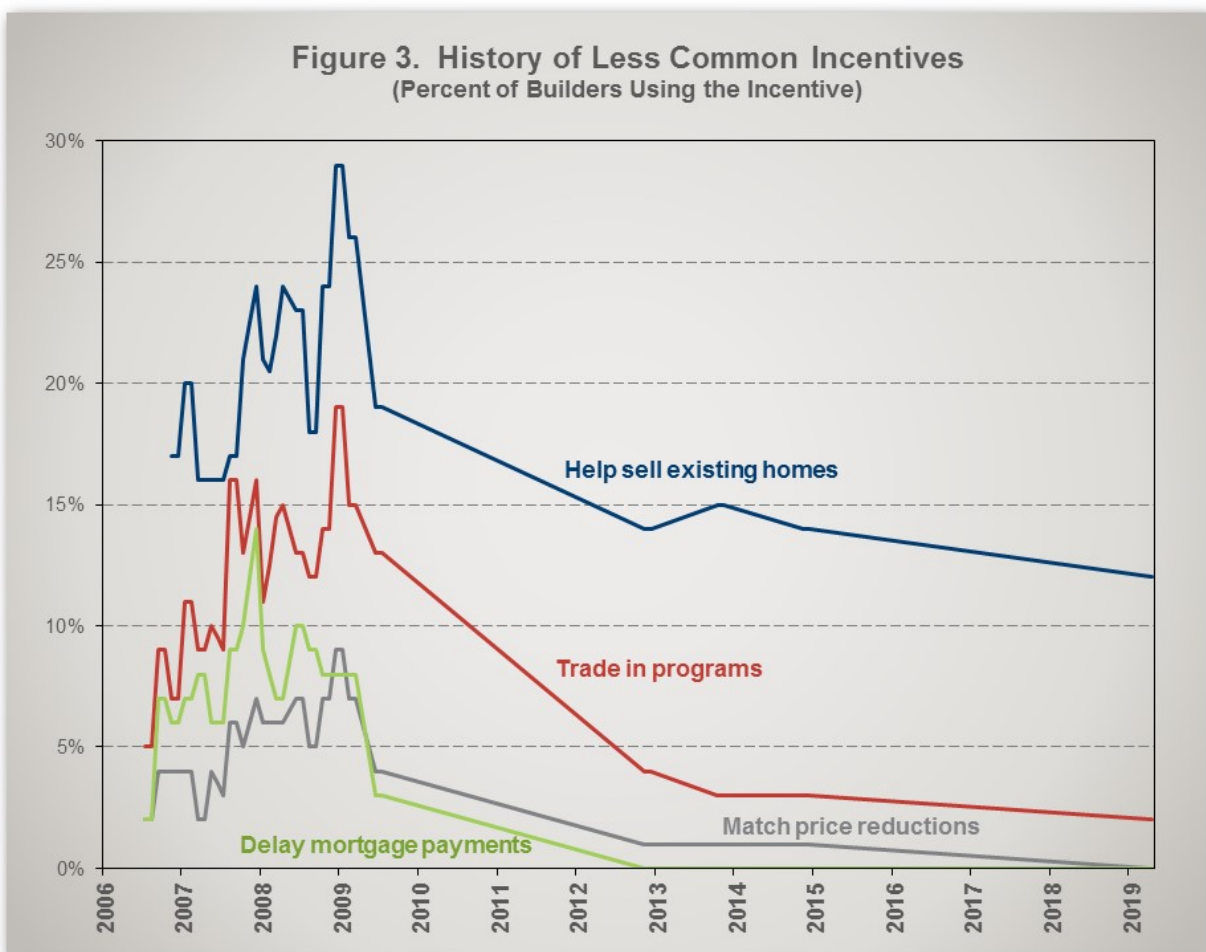
percent of builders (as reduced rates make less compelling advertising in the current low-interest environment). Builders' use of buy downs reached its peak (of 29 percent) at about the same time as the other incentives, in February of 2009 (fig. 2).



As incentives were becoming increasingly important in the market for new homes, NAHB added several new ones to the list in 2006. Among the new ones, “discounting home prices” turned out to be by far the most common. In fact, at its peak, 72 percent of builders were advertising discounted home prices in December 2008 and February 2009—making it the only incentive ever used by more than 70 percent of single-family builders. Then, as was the case for other incentives, the practice of advertising discounted home prices declined as the housing market recovered. As of 2019, “discounting home prices” is less common (at 26 percent)

than offering options or upgrades at reduced cost and paying the buyer's closing costs.

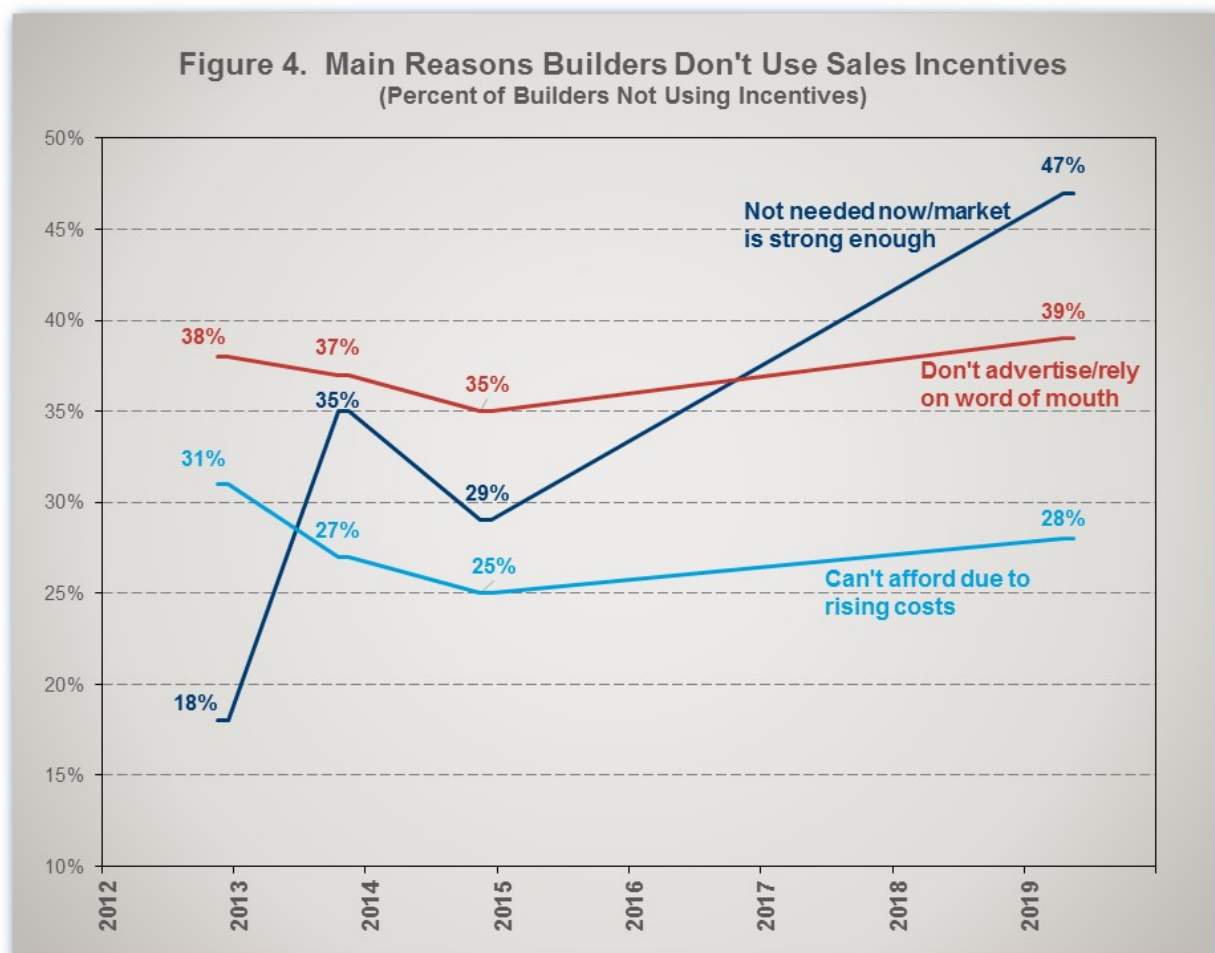
In addition to discounting home prices, other incentives added to the list in 2006 included "helping new home buyers sell their existing homes," "trade-in programs," offering to "match future price reductions" and "delaying mortgage payments." Like most of the incentives in fig. 2, the first three of these reached peaks in December of 2008 before subsequently declining. Offering to "match future price reductions" declined all the way to 0 percent in 2019. "Delaying mortgage payments" reached its peak (of 14 percent) a little earlier (in 2007), but subsequently declined very rapidly. No builders at all have reported delaying mortgage payments for their buyers since 2009 (fig. 3).



## Reasons Some Builders Don't Use Incentives

As noted previously, even in the depth of the latest downturn, some builders never turned to special incentives to help boost sales. Toward the end of 2012, NAHB began asking them why not. Initially, the most common reason was simply that some builders don't advertise. Either they are custom builders who specialize in building homes one-at-a-time and don't have tracts of homes to advertise, or rely on word-of-mouth or some other non-advertising method to generate leads, or both. Next to not-advertising, the most common reason for failing to offer incentives was that rising costs meant builders couldn't afford them.

In April of 2019 these motivations remained relatively common: 39 percent of the builders who don't use incentives cited simply not advertising as a reason, and 28 percent cited inability to afford them due to rising construction costs (fig. 4).

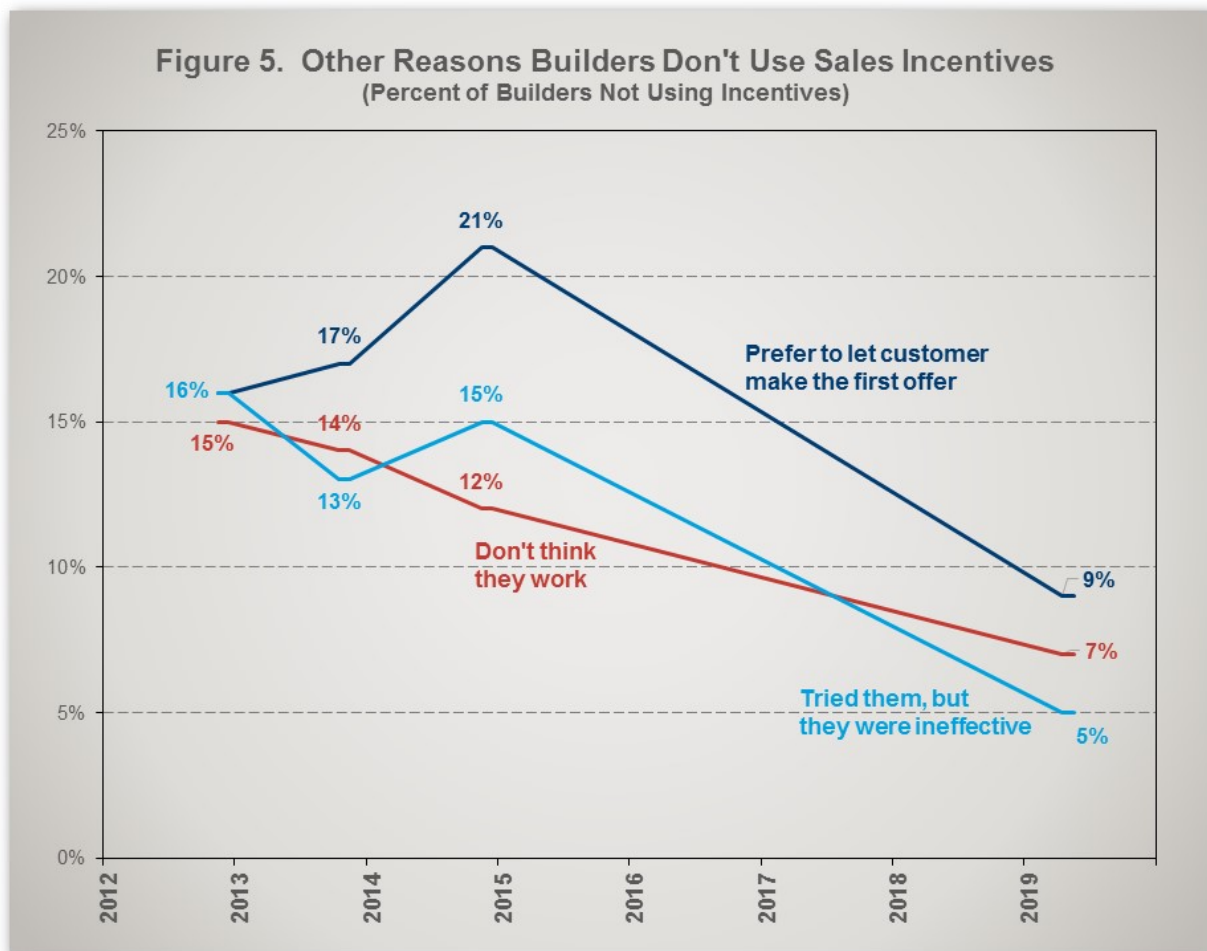


However, housing starts have continued to recover since 2012, going from under 800,000 to over 1.2 million in 2018. It may therefore not be surprising that the share of builders who reported not using incentives because the market is now strong enough so that they are not needed increased from 18 percent in 2012 to 47 percent in 2019.

It is important to remember that, even after all this, housing starts remain significantly below their long-term average. Over the four-decade period from 1963-2002 (which excludes the latest 2003-2006 boom period) starts averaged more than 1.5 million a year. In 2019, after a full decade of steady recovery, the seasonally adjusted annual starts rate is still struggling to keep its head above the 1.2 million water line.

There are a few other reasons builders don't use sales incentives, but they are less common, and have become even more so recently. As of April 2019, the shares of non-incentive using builders who avoid using them because they prefer to let the customer make the first offer, or don't think they work, or have tried them in the past without success have all fallen to under 10 percent (fig. 5).





## Summary and Conclusion

Advertising special incentives to help boost sales has been a normal part of business for many home builders for generations. Since 2000, however, use of these incentives has fluctuated significantly, along with overall activity in the housing market. During the boom period of 2003-2006, when home sales and single-family starts reached all-time highs and a disproportionate share of buyers consisted of speculators looking to flip homes quickly for short-term profit, use of incentives declined. During the subsequent downturn, use of incentives skyrocketed—to the point where over 70 percent of single-family builders were advertising discounted home prices in late 2008/early 2009.



If 2002, before the latest boom and bust cycle, represents a relatively normal period for the U.S. housing market, then use of incentives has returned to normal in 2019. Use of each of the five specific incentives NAHB has tracked in a consistent fashion has now returned to its 2002 level, or to a level that it crossed on its way down from 2002 to the 2003-2005 trough.

Consistent with this “return to normalcy” are the reasons some builders choose not to offer special sales incentives. The top reason, cited by 47 percent of builders not offering them in 2019, is a housing market that has recovered to the point where special incentives are no longer needed.